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RUEHGI/AMEMBASSY BANGUI 1316
RUEHEG/AMEMBASSY CAIRO 0136
RUEHKKH/AMEMBASSY KHARTOUM 0409
RUEHLC/AMEMBASSY LIBREVILLE 0972
RUEHLO/AMEMBASSY LONDON 1655
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UNCLAS SECTION 01 OF 03 NDJAMENA 000196

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SUBJECT: CHAD: 2007 BUDGET IN DANGER OF SLIPPING

REF: A) NDJAMENA 160, B) NDJAMENA 178

¶1. (SBU) Summary: The International Monetary Fund (IMF) and European Commission (EC) are concerned about the GOC's political will and capacity to meet agreed 2007 budget targets. Wage pressures, corruption and mounting military and off-budget spending -- combined with unrealistic assumptions of rising oil earnings -- increase the possibility of a return to insolvency by ¶2008. End summary.

Budget Overview

¶2. (U) The 2007 Government of Chad (GOC) Budget approved by the National Assembly in early February projects a CFA 229 billion (USD 458 million) surplus based on expenditures of CFA 689 billion (USD 1.4 billion) and revenue of CFA 918 billion (USD 1.8 billion). Revenue from oil taxes and fees are projected at CFA 166 billion (USD 332 million). Revenue estimates from foreign aid, grants and loans total some CFA 160.5 billion (USD 321 million) and include CFA 39.4 billion (USD 78.8 million) from bilateral foreign assistance, CFA 46.5 billion in international organization assistance (USD 93 million) and CFA 74.6 billion (USD 149 million) in international financial institution loans.

Revenue Projections Overstated

¶3. (SBU) Embassy officers met with European Commission (EC) financial analyst Charles Coste and an EC-funded technical advisor to the Ministry of Finance February 27 to discuss the budget. Coste described the budget as containing unrealistic projections of revenue and spending. Coste and the technical advisor described it as based on invalid base data and unrealistic revenue and spending assumptions. Coste added that the Ministry of Finance personnel who prepared the budget document were "prudent" and well-intentioned, but hampered by a lack of technical capacity and -- given the diversion of funds through large, unreported off-budget transfers -- lacked a basis upon which to make realistic projections. Coste noted that no attempt had

been made to develop a means of tracking oil receipts and warned that overall revenue projections could be overstated by as much as 50 percent.

14. (SBU) Coste added that 70 percent of non-oil budget revenue has been historically spent on salaries. Any large pay increase in 2007 bloating this recurring annual expenditure item would have to be largely financed by oil revenue and could only be sustainable in the unlikely event current oil production levels hold and prices in the volatile crude oil market remain high.

Defense and Off-budget Spending - From Surplus to Deficit

15. (SBU) Coste said that the IMF had estimated off-budget expenditures at CFA 50 billion (USD 100 million) in July 2006, but by October had increased the figure to CFA 97 billion (USD 194 million). Coste referred to mounting military and off-budget expenditures as the great unknown in Chadian government finances. By way of example, he said that large off-budget cash payments were made to Chadian army officers to entice them to engage in combat during the April 2006 rebel attack on N'Djamena. He claimed that general officers in particular received huge combat premiums. He claimed that payments of CFA 5 million (USD 10,000) are routinely paid to the families of soldiers of the Zaghawa and other select ethnic groups killed in combat and that the families of those seriously wounded

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received CFA 3 million (\$6,000).

16. (SBU) In addition to rising military expenditures, he cited contracts that were off-budget, single-source and open-ended as a major though unquantifiable drain on the government coffers. According to Coste, the practice of issuing major supply and infrastructure contracts without competitive bidding (referred to as the "simplified procedure") was common practice. He added that even when tenders were issued and bids invited, only a select group of suppliers and contractors close to President Deby responded. Because only the well-connected could be confident of being paid, others declined to bid on Chadian government tenders.

17. (SBU) Coste also cited graft and recurring payments to "former" rebels as major additional drains on the budget. Based on import data, he estimated that customs receipts in 2006 should have totaled CFA 150 billion (USD 300 million). Instead, the Ministry of Finance reported customs receipts of only CFA 40 billion (USD 80 million). He added that the growth of pension payments to former rebels was a long-term recurring liability. According to Coste, the December 2006 peace agreement with Mahamat Nour's FUC (United Front for Change) and other agreements with rebel groups dating back to 1991 have put large numbers of former rebels on the government dole as pensioners. Coste emphasized that many of the former rebels were pensioned off at young ages, had obviously never paid into a pension plan and could be expected to receive benefits into old age.

IMF Alarmed

18. (SBU) Previewing the upcoming visit of an IMF team (scheduled to arrive March 9), IMF representative Wayne Camard (please protect) reported that the 2007 budget was under severe pressure. In addition to military

spending, he pointed to unbudgeted big-ticket contracts (a dozen of which had apparently been signed directly by the President -- bypassing the Ministry of Finance), labor union demands for a minimum increase of 50 percent, pressure to "recapitalize" Cotontchad (paying off Cotontchad's large debt in one go rather than incrementally) and pressure to pay off internal debt and arrears.

¶9. (SBU) Camard said that the budgetary situation which the team will examine is "fragile." Were all of the pressures to come to bear, the government would not be able to stick to the agreed budget -- even with the "margin of safety" built into the 2007 budget. If the IMF were to declare Chad out of conformance, Chad would lose IMF budgetary support of USD 5 million and African Development Bank budgetary support of USD 10 million. While these sums in and of themselves were not enough to be a significant "carrot," Chad would also miss the HIPC completion point -- losing the chance to write off some \$1 billion in debt (half of which is owed to World Bank). Finally, although its portfolio has shrunk dramatically, thereby reducing its leverage, if the IMF left, the World Bank would be obliged to reassess its programs here.

¶10. (SBU) Camard commented that the Chadian government was in denial about the state of Chad's oil reserves and under the illusion that Chad is the next Equatorial Guinea. He warned that if the government continued on its current spending spree, it would draw down budget surpluses that are supposed to be retained to even out spending over the next couple of years. If the surplus was used up now, by 2008 the government would be unable to pay its bills, he warned.

¶11. (SBU) Comment: Public sector demands for a share of Chad's oil earnings through higher wages and rising

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military spending are the overt and immediate pressures on the 2007 government budget. A public sector wage increase of two percent provided for in the budget will likely lead to a general strike and the indefinite shutdown of all but essential government operations (Ref A). A more fundamental issue, however, is the lack of political will to be fiscally responsible. No amount of IMF, World Bank or bilateral technical assistance can lead to fiscal responsibility without the will to cease off-budget spending, cronyism and outright corruption. These are the real challenges. End comment.
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